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No. 88-2083

In the Supreme Court of the United States

OCTOBER TERM, 1989

LINCOLN HOMES, INC., AND JACK E. KOCH, PETITIONERS

v.

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION, AS RECEIVER FOR FIRST SOUTHERN SAVINGS ASSOCIATION OF JACKSON COUNTY, MISSISSIPPI

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether petitioners, who borrowed money from a savings and loan association that was subsequently placed in a Federal Savings and Loan Insurance Corporation (FSLIC) receivership, are precluded in a suit by FSLIC from defending against repayment of the loan on the basis of an alleged oral misrepresentation by an officer of the thrift.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-7a) is unpublished, but the decision is noted at 866 F.2d 1418 (Table). The opinion of the district court (Pet. App. 8a-12a) is unreported.

JURISDICTION

The court of appeals entered judgment on January 19, 1989. A petition for rehearing was denied on February 16, 1989. Pet. App. 16a. The petition for a writ of certiorari was filed on May 17, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Petitioners, who borrowed money from a savings and loan association that was subsequently placed in receivership, challenge the court of appeals' ruling that their claim of misrepresentation by the thrift was not valid against the receiver as a defense to repayment of the loan.

1. In 1985, petitioner Koch became interested in acquiring an uncompleted apartment complex located in Jackson County, Mississippi. The complex was encumbered by a deed of trust held by First Southern Savings Association of Jackson County, Mississippi. In December 1985, Koch and his company, petitioner Lincoln Homes, Inc., purchased the property. They assumed the outstanding indebtedness to First Southern and borrowed an additional $100,000 from First Southern for completion of construction. Petitioners gave First Southern an installment note for $535,000, secured by a deed of trust on the property. See Pet. 3; Pet. App. 2a.

Nothing in the note or in any other written document made repayment of the borrowed sum contingent on any appraisal of the property. Petitioners subsequently alleged, however, that First Southern's president orally indicated at the time of the loan transaction that the property had an appraised value sufficient to cover the debt. But petitioner Koch admitted at trial that there was not in fact any agreement that made the obligation to pay the note contingent on any appraisal of the property. Pet. App. 6a, 11a.

In the summer of 1986, petitioners defaulted on their payments on the note. They subsequently offered to deed the property to First Southern in lieu of the thrift's pursuing its foreclosure remedy. First Southern rejected the offer. Petitioners nevertheless issued, recorded, and mailed to the thrift a quitclaim deed to the property. Pet. App. 3a.

2. In February 1987, First Southern filed a complaint in the Chancery Court of Jackson County, Mississippi, asking the court to set aside the quitclaim deed issued by petitioners. The following month, the Federal Savings and Loan Insurance Corporation (FSLIC) was appointed receiver for First Southern. See Pet. 4.[1] FSLIC removed the case to the United States District Court for the Southern District of Mississippi, and it amended the complaint to seek the additional relief of foreclosure of the deed of trust and entry of a judgment against petitioners for any deficiency remaining after the sale of the property. See *ibid.*; Pet. App. 3a-4a.

Following trial, the district court set aside the quitclaim deed, appointed a special master to conduct a foreclosure sale of the property, and ordered that a deficiency judgment be entered for the balance of the indebtedness after the sale was completed. Pet. App. 8a-12a. The court held, contrary to petitioners' argument, that their attempted conveyance of the property by tendering the quitclaim deed was invalid because the offer was not accepted. *Id.* at 11a. The court also ruled that petitioners' claim of misrepresentation, based on the thrift president's statements regarding appraisal of the property, was not valid against FSLIC as a defense to repayment of the note. Without deciding whether any misrepresentation ever occurred (see *ibid.*), the court held that petitioners' defense was barred by the federal common law doctrine of *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942). Pet. App. 12a.[2]

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[1] Until August 9, 1989, FSLIC was the receiver for the thrift. On that date, the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, took effect. H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. (1989). Section 401(a)(1) of the Act abolishes FSLIC on the effective date of the Act. Section 401(f)(2) declares that suits by or against FSLIC shall not abate.

[2] A final judgment, which includes a deficiency assessment of more than $457,000, was entered against petitioners on March 1, 1989. Pet. App. 13a-15a.

3. The court of appeals, in an unpublished opinion, affirmed. Pet. App. 1a-7a. After rejecting petitioners' argument that the thrift had actually accepted the quitclaim deed (*id.* at 4a-5a), an argument that is not renewed in this Court, the court of appeals held that petitioners did not have a valid defense to repayment of the loan based on the alleged misrepresentation concerning the appraised value of the property. The court gave two reasons. First, as petitioner Koch himself testified at trial, repayment of the loan was never made contingent on any appraisal of the property. *Id.* at 6a. Second, even if the alleged misrepresentation constituted fraud in the inducement, the *D'Oench, Duhme* doctrine precludes petitioners from relying on it against FSLIC as a defense to repayment of the loan. That doctrine, the court explained, "operates to preclude debtors of federally insured financial institutions such as First Southern from raising defenses based on oral agreements with officers of those institutions that subsequently fail." *Ibid.*

ARGUMENT

Petitioners' challenge to the court of appeals' ruling that *D'Oench, Duhme* bars their misrepresentation defense is without merit and does not warrant this Court's review.

1. The court of appeals correctly applied the *D'Oench, Duhme* doctrine to petitioners' misrepresentation defense.[3] The courts have uniformly held that doctrine applicable to FSLIC even though, as petitioners note (Pet. 5), the doctrine has never been reflected in a statute applicable to FSLIC, whereas the doctrine does have a

[3] Neither of the courts below concluded that any misrepresentation ever actually occurred. And both courts noted that petitioners admitted that there was no agreement to make repayment contingent on appraisal of the property. Pet. App. 6a, 11a.

statutory counterpart—enacted after *D'Oench, Duhme* was decided—applicable to the FDIC, 12 U.S.C. 1823(e). See, *e.g., Mainland Sav. Ass'n* v. *Riverfront Assocs., Ltd.*, 872 F.2d 955, 956 (10th Cir. 1989), petition for cert. pending, No. 89-95; *Firstsouth, F.A.* v. *Aqua Const., Inc.*, 858 F.2d 441, 442-443 (8th Cir. 1988); *FSLIC* v. *Lafayette Inv. Prop., Inc.*, 855 F.2d 196, 198 (5th Cir. 1988); *Taylor Trust* v. *Security Trust Fed. S&L*, 844 F.2d 337, 342 (6th Cir. 1988)). And the *D'Oench, Duhme* doctrine's aims of protecting federal insurers, regulators, and receivers of financial institutions, and thereby indirectly promoting the integrity of the institutions and protecting their depositors and creditors, applies as strongly to thrifts, with FSLIC as insurer, regulator, and receiver, as to banks, with the FDIC in those roles.

Petitioners' defense comes within the scope of the doctrine. Their defense rests on the claim that they incurred their debt as a result of First Southern's fraudulent assurances that the property had a specified value. As this Court explained in *Langley* v. *FDIC*, 108 S. Ct. 396, 402 (1987), *D'Oench, Duhme* bars a borrower's assertion of a defense based on an arrangement with a financial institution that would "tend to deceive" or be "likely to mislead" the regulatory authorities, and "one who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to" just such an arrangement, "whether the condition consists of performance of a counterpromise (as in *D'Oench, Duhme*) or of the truthfulness of a warranted fact." Moreover, because it is mere tendency or likelihood to deceive regulatory authorities that triggers application of the doctrine, *D'Oench, Duhme* applies even though FSLIC may have known of the defense when it became receiver of First Southern.[4]

[4] None of the decisions cited by petitioners (Pet. 7-9) declined to ap-

2. The question of *D'Oench, Duhme*'s scope as applied to FSLIC is of little if any continuing importance. Under Section 401(a)(1) of the recently enacted Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73 (Aug. 9, 1989), FSLIC was abolished on August 9, 1989. See H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. 182 (1989). Moreover, all newly created federal-agency receiverships of federally insured depository institutions, as well as certain recently created receiverships, are covered by the newly amended version of 12 U.S.C. 1823(e).[5] Under *Langley*, that provision plainly bars the type of defense petitioners have raised, making reference to *D'Oench, Duhme* unnecessary. And for pre-Act receiverships like the one in the present case, even aside from the possible applicability of 12 U.S.C. 1823(e) to the successor receiver, the court of appeals' application

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ply *D'Oench, Duhme* because the receiver knew of the defense when it assumed that role.

Gunter v. *Hutcheson*, 674 F.2d 862, 873 (11th Cir.), cert. denied, 459 U.S. 826 (1982), did mention such knowledge in discussing the *D'Oench, Duhme* doctrine, but it merely noted the absence of such knowledge in holding that the doctrine did apply to the FDIC (in its corporate capacity) on the facts before it. In any event, *Langley*, decided after *Gunter*, both demonstrates that the result in *Gunter* should have been based on 12 U.S.C. 1823(e) (so that the Eleventh Circuit's reliance on *D'Oench, Duhme* was not necessary) and also makes clear that actual knowledge is not relevant to the statutory or common law protections.

[5] Section 217 of the new Act amends 12 U.S.C. 1823(e) to make it expressly applicable to notes acquired by the FDIC as receiver. That provision is also applicable to the Resolution Trust Corporation, which, among other duties, serves as successor receiver in cases where FSLIC was appointed receiver on or after January 1, 1989. § 501(a) (to be codified at 12 U.S.C. 1441a(b)(4)). Newly created federal receiverships have either the FDIC or the Resolution Trust Corporation as receiver. § 501(a) (to be codified at 12 U.S.C. 1441a(b)(4) and (6)); § 212(a) (to be codified at 12 U.S.C. 1821(c)).

of the *D'Oench, Duhme* doctrine to bar petitioners' defense is reinforced by the new Act's extension of Section 1823(e), which reaffirms the federal policies underlying the doctrine.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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